STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2001-178

July 10, 2001

CENTRAL MAINE POWER COMPANY
MAINECOM SERVICES
MAINE NATURAL GAS, LLC
MAINE ELECTRIC POWER COMPANY
CHESTER SVC PARTNERSHIP
Request For Approval of Affiliated Interest Transaction
For Two Service Agreements With Energy East
Management Corporation

ORDER APPROVING
STIPULATION

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY

In this Order we approve a stipulation submitted to us by Applicants and the Office of the Public Advocate which would grant waivers from certain requirements of Chapter 820 of the Commission's Rules and to approve the affiliate transaction agreements submitted by Applicants, with certain modifications, pursuant to the requirements of 35-A M.R.S.A. § 707.

II. BACKGROUND

A. Procedural History

On March 12, 2001, Central Maine Power Company (CMP), Maine Natural Gas, LLC (Maine Gas), Maine Electric Power Company (MEPCO), MaineCom Services (MaineCom), NORVARCO and Chester SVC Partnership (Chester) (collectively referred to us as Applicants) filed an application for approval of two service agreements pursuant to the provisions of 35-A M.R.S.A. § 707.

A Notice of Proceeding was issued on April 11, 2001. Timely petitions to intervene were filed by the Office of the Public Advocate (OPA) and the Industrial Energy Consumers Group (IECG) and were granted without objection. A petition for limited intervention was filed by Northern Utilities, Inc. which was also granted without objection.[1]

[1]Northern is a public utility engaged in the business of purchasing and distributing natural gas to retail customers in Maine. According to Northern, its primary interest in this case was monitoring the case for issues which could potentially impact it. Therefore, Northern stated that its intervention would be limited to receiving copies of all filings made in the proceeding and being permitted to participate further, at the Commission's discretion, with respect to particular matters, that may have a more direct effect upon Northern. CMP did not oppose to the intervention on the limited basis proposed by Northern.

A case conference on this matter was held on April 26, 2001. Based on discussions at the conference, a schedule allowing parties to ask discovery on the Applicants' filing and scheduling a follow-up technical conference was established by the Hearing Examiner on May 1, 2001. Written data requests were issued by the OPA and the Commission's Advisory Staff and were answered by the Applicants. A technical conference was held, as scheduled, on June 6, 2001 at which time Applicants' representatives responded to questions from the Advisory Staff and from the parties.

On June 22, 2001, CMP and the OPA filed a stipulation proposing to resolve all issues in this matter. In the cover letter to the stipulation, counsel for CMP indicated that the Industrial Energy Consumers Group, the only other party, would not be signing the stipulation but would not be requesting a hearing. The letter did not indicate whether the IECG wished to file written comments or objections on the stipulation. By way of the Procedural Order dated June 26, 2001, the IECG was given until June 29, 2001 to file written comments or objections to the stipulation. On July 2, 2001 the IECG submitted late-filed comments in opposition to the proposed stipulation.

B. Description of Agreements

In their Application for Approval of Affiliated Interest Transactions, the Applicants request approval for two forms of service agreements. Under the first agreement (Agreement A), Energy East Management Corporation (EE Management), a subsidiary of Energy East Corporation (Energy East), provides certain centralized support services to Applicants. Under Agreement A it anticipated that Energy East Management may provide the following services:

- Accounting services, such as the maintenance of Energy East books and records, preparation of financial and statistical reports, tax filings and supervision of compliance with applicable laws and regulations;

- Audit services and management of an entity-wide framework of corporate controls;

- Corporate planning services, such as the preparation of corporate plans, budgets and financial forecasts, monitoring trends and evaluating business opportunities;

- Executive services, such as providing general management and strategic planning;

- Finance and treasury services, such as coordinating activities relating to securities issuances, cash management services, investing activities, monitoring capital markets, performing financial and economic analysis and administering insurance programs;

- Governmental affairs services, such as lobbying governmental officials and monitoring, reviewing and researching legislation;

- Human resource services, such as establishing and administering policies and supervision of compliance with legal requirements in the areas of employment, compensation, benefits and employee health, welfare, and safety, processing of payroll and employee benefit payments, and the coordination of contract negotiation and relations with labor unions;

- Legal services coordination among law and regulatory departments within the Energy East system; and

- Other corporate support services, which may include information/telecommunication services, purchasing, contract administration, and corporate communications.

Under the second form of agreement (Agreement B), Applicants would be providing services to each other or to other companies in the Energy East registered holding company system that are incidental to their utility business or that require the specialized expertise of a utility employee. Under the terms of Agreement B, the Applicants may provide to or receive from one another various types of operational services, including call center operation, customer billing network support services, information services, credit and collection services, as well as the management support services.

Under both agreements, services would be charged at fully distributed cost (FDC). Under the FDC methodology all labor, material and other expenses would be directly charged to the receiving entities whenever possible. Where costs cannot be directly charged costs are to be allocated based upon a measurable cost driver. Under the Cost Allocation Manual to be used in Agreement A, direct labor time is to be measured in one-hour increments, while under the Cost Allocation Manual to be used in Agreement B labor is to be measured in 15-minute increments.

The Applicants note that FDC cost methodology is required by the Securities and Exchange Commission (SEC) under the Public Utilities Holding Company Act (PUHCA) and that the SEC has, in approving the creation of EE Management, approved the two forms of agreements submitted here. In addition, the Applicants argue that while Chapter 820 requires market price, Energy East and Applicants do not sell these services outside the Energy East family. Therefore there is no market price or, in the case of the Applicants, any tariffed ratemaking the FDC methodology appropriate.

EE Management and Energy East are affiliated interests of Applicants and the Applicants are public utilities in Maine and are affiliated interests of one another under the provisions of 35-A M.R.S.A. § 707. Therefore, Commission approval of Agreement A and Agreement B are required under the provisions of 35-A M.R.S.A. § 707(3).

C. Description of the Stipulation

The stipulation makes several material changes to the agreements submitted for approval. First, the stipulation changes language in both Agreement A and B which would allow the Applicants and Energy East Management to add to the services listed without further approval. The stipulation limits the services in the agreements approved here to those services specifically listed in the agreements and to special services which do not materially add to those services listed and which the providing entity concludes it is able to perform. In addition, under the terms of the stipulation, Energy East Management shall amend its cost allocation manual so that actual labor charges shall be tracked and reported in 15-minute increments.

Finally, the parties to the stipulation recognize that market pricing is either required or preferred with respect to service billings among members of an affiliated group under the provisions of Chapter 820 of the Commission's Rules. However, given the SEC's requirement to follow FDC for services provided among members of the Energy East corporate group and that CMP, by far the largest applicant of those to receive services, is currently under a seven-year Alternative Rate Plan (ARP) where CMP's rates are adjusted pursuant to a formula rather than pursuant to traditional ratemaking, the parties agree that a waiver from the requirements of Chapter 820 in this instance is appropriate. The waiver shall permit Energy East Management to bill Applicants no more than $7 million during any calendar year. To the extent that Applicants seek to increase this amount to no more than $10 million, they shall make a notice filing with the Commission and the increase shall automatically become effective unless, within 20 days of such filing, a party to this proceeding or the Commission's Staff files an objection to the increase which shall fully set forth the reasons for such objection. To increase the waiver amount above $10 million, the Applicants shall file a request with the Commission explaining the reasons for such increase. The Commission shall act upon any objection described in this subparagraph within 60 days of the filing and shall act upon a request to increase the waiver amount above $10 million within 120 days of the filing.

The stipulation goes on to provide that:

> For ratemaking purposes, each of the applicants will provide appropriate market information (which shall mean market rates for such services or, of the applicants conclude that no market rates are available, the explanation supporting the unavailability of market rates) to demonstrate that the costs billed under these agreements are just and reasonable. Such market information shall only be required if and to the extent that an applicant is seeking (or another party is requesting) a rate change (whether in a general rate proceeding, pursuant to a bottom-end earnings sharing mechanism, or as a result of a mandated cost) that includes costs billed under the agreements approved herein. In such a proceeding seeking a rate change, any other party is free to contest the reasonableness of the costs incurred under the agreements approved herein and the applicant seeking

> to include such costs in its rate change shall have the burden of proof as to the reasonableness of such costs.

Stipulation, para. 5(b).

III. DECISION

As we have now stated on many occasions, to accept a stipulation the Commission must find:

1. the parties joining the stipulation represent a sufficiently broad spectrum of interests that the Commission can be sure that there is no appearance or reality of disenfranchisement;

2. the process that led to the stipulation was fair to all parties; and

3. the stipulated result is reasonable and is not contrary to legislative mandates.

See Central Maine Power Company, Proposed Increase in Rates, Docket No. 92-345(II), Detailed Opinion and Subsidiary Findings (Me. P.U.C. Jan. 10, 1995), and *Maine Public Service Company, Proposed Increase in Rates (Rate Design),* Docket No. 95-052, Order (Me. P.U.C. June 26, 1996). We have also recognized that we have an obligation to ensure that the overall stipulated result is in the public interest. *See Northern Utilities, Inc., Proposed Environmental Response Cost Recovery,* Docket No. 96-678, Order Approving Stipulation (Me. P.U.C. April 28, 1997). We find that the proposed Stipulation in this case meets these criteria.

The Stipulation before us was entered between the Company and the OPA. In past cases, we have found that these two entities, representing often opposite views in the ratemaking process, constitute a sufficiently broad spectrum of interests to satisfy the first criteria. *See Public Utilities Commission, Investigation of Stranded Cost Recovery, Transmission and Distribution Utility Revenue Requirements and Rate Design of Bangor Hydro-Electric Company (Phase II),* Docket No. 97-596, Order at 6 (Feb. 29, 2000) and *Maine Public Utilities Commission, Investigation of Retail Electric Transmission Services and Jurisdictional Issues,* Docket No. 99-185, Order Approving Stipulation (Maine Public Service Company) at 3 (Aug. 11, 2000). In this case, we also note that our Advisory Staff was an active participant in the settlement process and has not indicated any objection to the Stipulation. We are, therefore, satisfied that a broad spectrum of interests are represented by the stipulation.

We also find that the second criterion has been met in this case. The case schedule, which primarily relied on informal technical and settlement conferences rather than formal hearings as a means of developing the record, was developed with the input of all parties. In addition, all parties were provided with an opportunity to conduct formal written discovery on the Applicants. Our review of the procedural history in this case then indicates that all procedural safeguards were satisfied in this instance. We next address then whether the stipulation is reasonable, meets our legislative mandates and is in the public interest.

Chapter 820 of our rules requires that any utility service or personnel used by an affiliate shall be charged to the affiliate at the tariffed rates, if available, or in the absence of a tariffed rate at the market price, if available, or otherwise at fully distributed cost. MPUC Rules, ch. 820, § 4(A). For personnel of an affiliate used by a utility the price is to be the same price charged to non-affiliates. If no such price is available, then such services or use of personnel should be priced at the market price. MPUC Rules, ch. 820, § 4(E).

Unquestionably then, Chapter 820 clearly expresses a preference for market prices. Section 9 of Chapter 820, however, provides that the Commission may waive the requirements of Chapter 820 upon a finding of good cause and that the waiver would not be inconsistent with the requirements of sections 707, 708, 713, 714 and 715 of Title 35-A. Based on the circumstances present here and with the conditions set forth in the stipulation, we conclude that good cause exists for the waiver of Chapter 820's requirements for market price costing.

Specifically, we first note that Energy East is required to follow the fully distributed cost methodology pursuant to SEC requirements. The fact that the fully distributed costing will be subject to SEC scrutiny and will be done subject to cost allocation manuals reviewed by both the SEC and our Staff provides us with some degree of comfort that the costing will not be done arbitrarily or capriciously.

More importantly CMP, by far the largest of Applicants in terms of costs and revenues, is now operating under the ARP 2000 rate plan approved by the Commission in *Central Maine Power Company, Request for Approval of Alternative Rate Plan (Post-Merger) "ARP 2000,"* Docket No. 99-666, Order Approving Stipulation (Nov. 16, 2000). Under ARP 2000, CMP's rates as a general matter will be based on an external index (inflation – productivity) for the next six and one-half years. Thus, not only are CMP's affiliate transaction costs irrelevant to the rates set under the general index but more importantly CMP has a direct incentive to find the most efficient and cost-minimizing way to provide service as opposed to the incentive presented by traditional cost-plus regulation to shift costs among affiliates in ways which maximize recovery from the utility's ratepayers.[2] To the extent that rates may actually be influenced by the affiliate transaction costs under the proposed agreements, the stipulation requires the utility to either provide market prices for services or a specific explanation why market prices cannot be provided. The stipulation also provides that Energy East may only bill Applicants up to $7 million in any one calendar year under the waiver without further Commission approval.

We find that good cause exists for the proposed waiver, that the waiver is not inconsistent with the purposes of Chapter 820 or with the requirements of sections 707, 708, 713, 714 and 715 of Title 35-A. Therefore, we conclude that the waiver request

[2]The ARP 2000 plan contains a Service Quality Index to ensure that costs are not minimized at the expense of service quality. To the extent that additional service quality protections are required such issues may be considered by the Commission as part of the mid-period review.

contained in the stipulation is reasonable and consistent with the requirements of Chapter 820, § 9.

We further find that the affiliate agreements, as modified by the stipulation, are not adverse to the public interest and thus find the stipulation's provisions that we approve both Agreement A and Agreement B, as modified, to be consistent with legislative mandates and with the public interest. Specifically, the stipulation, with certain limited exceptions, limits the services to be provided to those listed in the agreements. In addition, to ensure the accurate allocation of time to particular projects, EE Management has agreed to amend its cost allocation methodology so that actual labor charges are to be billed in fifteen-minute increments as opposed to hourly increments as originally proposed. With these changes and with the protections incorporated into the conditions for the granting of the Chapter 820 waiver, we conclude that the stipulation satisfies the requirements of 35-A M.R.S.A. § 707, is in the public interest and should be approved.

Accordingly, it is

O R D E R E D

1. That the stipulation filed by the Applicants and the Office of the Public Advocate on June 22, 2001 in this matter, a copy of which is attached hereto and marked as Exhibit A, is approved;

2. That the Applicants shall file the affiliate transaction agreements as modified by the stipulation in compliance with this Order;

3. That approval of this compliance filing is delegated to the Director of the Commission's Finance Division; and

4. That pursuant to the requirements of 35-A M.R.S.A. § 707(D), approval of the agreements, as modified by the stipulation, does not limit or restrict the powers of the Commission in setting rates under the provisions of Title 35-A.

Dated at Augusta, Maine, this 10th day of July, 2001.

BY ORDER OF THE COMMISSION

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Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Diamond

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Appellate Procedure.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.